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IN THE
Supreme Court of the United States

DANIEL HEIMMERMANN AND EMILY HEIMMERMANN, BOTH INDIVIDUALLY AND ON BEHALF OF THEMSELVES AND ALL OTHERS SIMILARLY SITUATED,
Petitioners,
v.
FIRST UNION MORTGAGE CORPORATION,
Respondent.

BETH A. RICHARDSON AND PAMELA C. HIRSCH, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED, DAVID L. HIRSCH,
Petitioners,
v.
BANKAMERICA CORPORATION, A DELAWARE CORPORATION, BANK OF AMERICA FSB, INC., A HAWAII CORPORATION, BANKAMERICA MORTGAGE, A DIVISION OF BANKAMERICA FSB, A HAWAII CORPORATION,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

BRIEF OF NATIONAL ASSOCIATION OF CONSUMER ADVOCATES AND PUBLIC CITIZEN AS *AMICI CURIAE* IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the Eleventh Circuit erred in according *Chevron* deference to an informal Department of Housing and Urban Development ("HUD") policy statement, the explicit purpose of which was to overrule the Eleventh Circuit's own precedent in this case, given that: (i) The Eleventh Circuit had previously held the same legal interpretation as later espoused by the policy statement to be contrary to the clear language and an unreasonable interpretation of the statute; and (ii) the deference accorded by the Eleventh Circuit to HUD's informal agency policy statement conflicts with seven other circuits that have denied agencies the authority to use policy pronouncements to overrule circuit precedent.

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INTEREST OF *AMICI CURIAE*[1]

The National Association of Consumer Advocates ("NACA") is a membership organization consisting of private and public sector attorneys, legal services attorneys, law professors, and students whose primary practices and areas of specialty involve consumer protection issues. NACA was a member of the Negotiated Rulemaking Advisory Committee on Mortgage Compensation and Disclosure of the Department of Housing and Urban Development ("HUD").

Public Citizen is a national consumer organization with approximately 125,000 members. This organization has a long-standing interest in preventing large institutions (including the Federal Government) from compelling consumers and workers to forgo remedies. It believes the Court should grant review because the rights that Congress sought to protect under the Real Estate Settlement Procedures Act of 1974 will be undermined if the Eleventh Circuit's decision stands.

Amici further believe that the approach taken by the Eleventh Circuit, to afford *Chevron* deference to an informal agency policy statement and thereby require the overruling of circuit precedent, accords far too much power to administrative agencies selectively to adhere to decisions by courts of appeals. Under the Eleventh Circuit's approach, an agency can simply reverse a court of appeals decision through an agency statement that has no input from the public, no formal notice and comment opportunity, and none of the other indicia of law.

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[1] Pursuant to Supreme Court Rule 37.6, counsel for *amici* represents that it authored this *amicus* brief and that no entity other than *amici*, their members, or their counsel made a monetary contribution to the preparation or submission of the brief. Counsel for *amici* represents that counsel for all parties have consented to the filing of this *amicus* brief. Letters reflecting their consent have been filed with the Clerk.

STATEMENT

Buying and financing a home is a typical consumer's largest and most complex financial transaction.[2] The complexity of the transaction and the infrequency of the average homeowner's experience with mortgage transactions make consumers especially vulnerable to being overcharged for loan origination services.[3] The broad array of loan products now available to consumers has rendered the home purchase and mortgage process significantly more complicated and confusing.[4] As a result, the average residential borrower must rely on the mortgage broker or a loan officer when choosing mortgage products. Yet the industry promotes a secret incentive system designed to encourage brokers to recommend higher interest rate loans that will result in fees to brokers that are wholly unrelated to whether anything is owed to the broker for its services.

Kickbacks and referral fees are a commonplace, long-standing practice in the residential mortgage industry. *See* Paul Barron, *Federal Regulation of Real Estate and Mortgage Lending* ¶ 2.04, at 2-25 n.1 (3d ed. 1992). Congress attempted to end those practices in 1974 when it enacted the Real Estate Settlement Procedures Act ("RESPA"), 12 U.S.C. §§ 2601 *et seq.*, which contains a prohibition against the giving or receiving of "any fee, kickback, or thing of value pursuant to any agreement or

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[2] *See* Testimony of Gail Laster, General Counsel, U.S. Department of Housing and Urban Development, Before the Subcomms. on Financial Institutions and Consumer Credit and on Housing and Community Opportunity of the House Comm. on Banking and Financial Services, 105th Cong. (July 22, 1998).

[3] *See, e.g.*, S. Rep. No. 93-866 (1974), *reprinted in* 1974 U.S.C.C.A.N. 6546, 6547 (consumers' lack of understanding about the settlement process and its costs makes it difficult in a free market for settlement services to function at maximum efficiency).

[4] *See* Testimony of James McCabe on behalf of the Mortgage Bankers Association of America Before the Subcomm. on Housing and Community Opportunity of the House Comm. on Banking and Financial Services, 105th Cong. (Mar. 27, 1998).

understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person." 12 U.S.C. § 2607(a).

In 1992, after the emergence of the mortgage brokerage industry, Congress amended RESPA to make it expressly applicable to mortgage originations. At that time, HUD did not take a position on the legality of yield spread premiums. *See Real Estate Settlement Procedures Act (RESPA) Statement of Policy 1999-1 Regarding Lender Payments to Mortgage Brokers*, 64 Fed. Reg. 10080, 10082 (1999) ("1999 Policy Statement") (Pet. App. 137a). HUD did, however, issue rules requiring that all payments to brokers be disclosed, including yield spread premiums. *See* 12 U.S.C. § 2603(a); 24 C.F.R. Pt. 3500, App. A. This requirement caused an uproar in the mortgage industry, which claimed that consumers "did not benefit from the disclosure [of yield spread premiums]" because disclosure of such "indirect" fees would "confuse" and "mislead" borrowers. *See* 1999 Policy Statement, 64 Fed. Reg. at 10083 (Pet. App. 139a).[5]

A substantial number of borrowers obtain home mortgage financing by securing the services of a mortgage broker. *See id.* at 10080. These brokers provide some services to borrowers, such as completing standard loan applications, helping obtain appraisals, getting credit reports, and providing all origination services necessary to present a fundable loan. Importantly, mortgage brokers do not fund the mortgage loans that form the basis of this litigation and, therefore, do not own the loans at the time of closing. Loans originated by mortgage brokers, but funded by mortgage lenders, such as Respondents First Union and BankAmerica, are known as "table-funded" transactions.

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[5] A former HUD employee has described his experience of receiving more than 2,000 letters from mortgage brokers protesting HUD's suggestion that brokers should mention yield spread premiums on the federally mandated HUD-1 disclosure form. Grant E. Mitchell, *RESPA the Inside Story*, 60 Mortgage Banking 26, 1999 WL 12029502 (Nov. 1, 1999).

24 C.F.R. § 3500.2. In table-funded transactions, brokers steer borrowers to one of the many lending institutions with which the broker has a standard contractual relationship.

Each day lenders will send their brokers a "rate sheet" showing the interest rates at which the lenders are willing to loan money. The rate sheet constitutes the lender's agreement to pay a specified fee in exchange for the broker's referral of an inflated interest rate, or above-par, loan.[6] The more an interest rate exceeds the par rate on a particular loan, the greater the amount of the yield spread premium paid to the broker. In this manner, lenders reward brokers for sending them business where the borrower has been assessed an above-market interest rate. The mortgage broker decides the terms of the transaction from among the options offered on the rate sheet. This includes determining what the interest rate will be on that particular transaction by reference to the rate sheets. The borrower is prohibited by the lender from seeing these rate sheets and cannot therefore learn of the availability of better interest rates or the costs of accepting a higher interest rate.

Mortgage brokers are paid for their services in a variety of ways. They usually charge a "loan origination fee" to compensate them for their work in helping to arrange the loan. They also charge specific fees for certain services such as document preparation fees, processing fees, and application fees. These fees are usually paid directly by the borrower at closing.

Brokers also commonly receive indirect compensation from the lenders with whom they have referral agreements. These payments are referred to variously as "yield spread premiums," "service release premiums," or "back funded payments." 1999 Policy Statement, 64 Fed. Reg. at 10081.

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[6] A "par loan" is a loan that a lender will fund at 100 cents on the dollar, as shown on the rate sheet. An "above-par loan" is one that is placed at an interest rate higher than "par" and for which the lender is willing to pay more than 100 cents on the dollar.

These fees are based upon the interest rate that the broker locks in for the lender.

SUMMARY OF ARGUMENT

Petitioners collectively seek redress for a violation of RESPA. By denying their right to proceed as a class, the Eleventh Circuit has made it impossible, as a practical matter, for a court to determine whether the practices of mortgage lenders such as Respondents violate RESPA. Borrowers and their counsel have little incentive to pursue claims that range from $500 to $2,500, particularly in light of the heavy discovery burden required by the "reasonableness" liability test adopted by the Eleventh Circuit.

Section 8 of RESPA contains a broad, straightforward prohibition against kickbacks and referral fees. Petitioners contend that Respondents' practice of paying yield spread premiums to mortgage brokers violates this prohibition. This question is appropriate for determination on a classwide basis because the practices of Respondents are uniform as applied to all putative class members.

The sole basis for the Eleventh Circuit's decertification order was its deference to HUD's 2001 "Clarification" of its Policy Statement. *See* 1999 Policy Statement, 64 Fed. Reg. 10080 (1999); *Real Estate Settlement Procedures Act Statement of Policy 2001-1: Clarification of Statement of Policy 1999-1 Regarding Lender Payments to Mortgage Brokers, and Guidance Concerning Unearned Fees Under Section 8(b)*, 66 Fed. Reg. 53052 (2001) ("2001 Policy Statement"). This 2001 Policy Statement states that, in determining whether there has been a violation of RESPA's prohibition against referral fees, each transaction must be looked at individually to determine whether the amount of the yield spread premium is "reasonable" considering the total compensation paid to the broker. HUD's rationale in its 2001 Policy Statement seeks to prohibit courts from employing the just and efficient class action mechanism to resolve hundreds of thousands of identical consumer claims

arising from the same course of corporate conduct and arising under the same federal statute.

In ruling as it did, the Eleventh Circuit has given HUD's 2001 Policy Statement the force of law. However, this policy statement did not result from any formal rulemaking process, such as a notice and comment procedure, that would have allowed *amici* and others to be heard. In fact, HUD's 2001 Policy Statement, on which the court below based its ruling, was the result of pressure from the industry to respond to and attempt to reverse the effect of the Eleventh Circuit's earlier *Culpepper III* decision, which properly interpreted RESPA's statutory language. *Culpepper v. Irwin Mortgage Corp.*, 253 F.3d 1324 (11th Cir. 2001), *cert. denied*, 534 U.S. 1118 (2002).

HUD, in its 2001 Policy Statement, has effectively conferred upon itself the very rate-setting authority that Congress specifically considered, and rejected, in enacting RESPA, by requiring an inquiry into the reasonableness of a broker's total compensation as a prerequisite to determining whether a yield spread premium violates RESPA § 8(a). Indeed, the Fourth Circuit has recently rejected HUD's attempt, through the same 2001 Policy Statement at issue here, to transform RESPA § 8(b) into a rate-setting statute. *See Boulware v. Crossland Mortgage Corp.*, 291 F.3d 261 (4th Cir. 2002). And the Seventh Circuit has, in direct conflict with the decision below, rejected the notion of giving *Chevron* deference to HUD's 2001 Policy Statement. *See Krzalic v. Republic Title Co.*, 314 F.3d 875 (7th Cir. 2002).

HUD's 2001 Policy Statement is itself based on the false assumption that borrowers "choose" to pay yield spread premiums in order to finance the payment of settlement costs and fees instead of paying them directly. The mortgage broker industry has consistently and vigorously resisted any meaningful disclosure to borrowers about the existence or effect of yield spread premiums. Yield spread premiums are classic kickback payments for referrals

exchanged between lenders, such as Respondents, and their network of brokers. The borrowers are not participants in or cognizant of these kickback arrangements. Instead, as Congress recognized, borrowers such as the Heimmermanns, Hirsches, and Richardson are the victims of this practice and suffer the resulting increased home loan costs.

ARGUMENT

I. YIELD SPREAD PREMIUMS ARE DESIGNED TO ENCOURAGE BUSINESS REFERRALS, NOT TO FINANCE CLOSING COSTS

A. Yield Spread Premiums Are Marketed And Designed To Promote Business Referrals

The mortgage industry's own representatives admit that yield spread premiums are a "method of enticing mortgage brokers to refer loans to lenders." Robert A. Cook, *Yield Spread Premiums Come Under Attack*, 48 Consumer Fin. L.Q. Rep. 94 (1994). Similarly, counsel for the National Home Equity Mortgage Association ("NHEMA") explains on NHEMA's website that the "uncertainty" surrounding the legality of yield spread premiums hurts lenders that refuse to pay yield spread premiums because they "lose market share." *See* Joe Lefkoff, *HUD Continued Inaction Contributes to the Chaos Associated with RESPA* (1997), *at* www.nhema.org/hudrespa.htm. Payment for referring a borrower to settlement service providers, such as lenders, is precisely what RESPA prohibits. It would be difficult to imagine a practice that is more questionable under the law and that affects more consumers than the subject yield spread premium practice.[7]

The mortgage industry's own lawyers warned long ago that the practice of paying yield spread premiums was dubious at best. More than six years ago, one industry lawyer warned:

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[7] Given the volume of mortgage business done by BankAmerica and First Union, it would not be surprising if hundreds of thousands of consumers are adversely affected by their practices.

> Some lenders pay an "overage" to a broker or dealer for "up-selling the rate." This refers to additional payments by an equity lender to a broker for a loan that has a higher-than-expected rate of interest. The extra payment from the equity lender is intended to compensate the broker for bringing to the lender such an attractive, high rate loan. *If a RESPA Sec. 8 violation is asserted, it is debatable whether an equity lender can defend payment of the extra overage money as payment of a thing of value for services rendered.*

Leonard A. Bernstein, *RESPA Invades Home Equity, Home Improvement and Mobile Home Financing*, 48 Consumer Fin. L.Q. Rep. 194, 197 (1994) (emphasis added).

Another industry attorney issued even stronger warnings to the lending and brokerage industry that the practice of paying yield spread premiums in table-funded loans violates RESPA's anti-kickback provisions:

> It is my opinion that three compensation practices — back end points, yield spread differentials and service release fees — are prohibited and illegal. . . . Yield differentials in which pay is based upon the difference between the rate obtained by the broker and the rate at which the lender would otherwise be willing to make the loan can be even more "explosive." . . . [T]he only bona fide way to base compensation on yield differentials, which are sometimes known as overages, is if the deal is clearly a secondary market transaction. If, on the other hand, the lender is table funding the loan, he is violating RESPA Sec. 8 anti-kickback provisions.

HEL Lenders May Be Sued On Broker Referrals, National Mortgage News at 111 (Apr. 3, 1995); *see also* Joe Lefkoff, *Traditional Broker Compensation Under RESPA: Is it Legal?*, Equity Magazine at 18 (Dec. 1994) ("While a yield spread is permitted and justifiable in a secondary market transaction, it is a prohibited fee for referral in the table funded or broker referral situation. The payment, while

measured by the yield spread, is for the referral."). Since the inception of this practice, the use of yield spread premiums has been acknowledged as highly suspect by industry and consumer representatives. The availability of a class action thus provides an opportunity to resolve efficiently the legality of the type of yield spread payments made by Respondents and other lenders.

B. Respondents Misrepresent Consumer Choice In Today's Marketplace

The simple duplicity of Respondents' contention that consumers "choose" to pay yield spread premiums in exchange for lower up-front payments is obvious from the fact that the mortgage industry continues to hide yield spread premiums from borrowers. Yield spread premiums are often "disclosed" on the HUD-1 Settlement Statement with designations such as "$2,000 yield spread premium to Broker POC."[8] Richardson's HUD-1 makes reference to a "Premium Pricing to POC (600.00) from B of A to AMM [Atlanta American Mortgage]." Pet. App. 91a (line 811). As HUD has recognized, these cryptic "disclosures" mean nothing to the average borrower. *See* 1999 Policy Statement, 64 Fed. Reg. at 10087. They certainly are not consistent with Respondents' claim that yield spread premiums are presented to borrowers as a financing option.

II. THERE IS NO SUCH THING AS A "REASONABLE" REFERRAL FEE UNDER RESPA

Nothing in the text or legislative history of RESPA supports Respondents' position that a lender's payment of a referral fee is not a referral agreement made illegal under RESPA § 8(a) so long as the broker performs some specified work for the borrower and the total compensation that the broker receives is "reasonable." The words "total compensation" and "reasonable" are not even in § 8(a) or (c)

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[8] Translation: The lender has made a payment outside closing ("POC") of $2,000 to the broker and that payment was calculated by the yield spread premium.

of RESPA. Such an analysis simply stands RESPA's prohibition against kickbacks and referral fees on its head. The statute prohibits *all* kickbacks and referral fees — no matter how great or small their cost and no matter how great or small the broker's "total compensation." Nothing in the plain text of § 8(a) or (c) supports a reading that a referral fee becomes legal simply because it is part of an overall fee paid to a broker that is "reasonable."

Moreover, the legislative history of RESPA demonstrates clearly that Congress sought to outlaw certain practices and refused to empower HUD to police the reasonableness of settlement fees. In 1970, Congress adopted § 701 of the Emergency Home Finance Act, which charged HUD and the Veterans Administration with the task of prescribing standards governing the amount of closing costs on FHA-insured and VA-guaranteed loans. S. Rep. No. 93-866 (1974), *reprinted in* 1974 U.S.C.C.A.N. 6546, 6558. A joint HUD/VA study was completed in 1972, which documented an elaborate system of referral fees, kickbacks, rebates, commissions and the like as an inducement to those firms and individuals who direct payment of business and urged Congress to take immediate action to prevent such kickbacks by establishing maximum allowable settlement charges on FHA-VA transactions in specific housing market areas. *Mortgage Settlement Costs: Report of the Department of Housing and Urban Development and Veterans Administration* 3 (Mar. 1972) (Comm. Print of the Senate Comm. on Banking, Housing and Urban Affairs, 93d Cong., 2d Sess.).

Congress considered two bills aimed at addressing the problems identified in the HUD/VA Report, which differed with respect to the authority of HUD and the VA to regulate charges for settlement services. One bill regulated closing costs directly by placing a ceiling on the charges that could be imposed in a real estate closing of any federally related home loan, while the second bill regulated the underlying business relationships and procedures of which the costs were a function. In enacting RESPA,

Congress chose the second approach. *See Real Estate Settlement Costs: Hearings on H.R. 9989 Before the Subcomm. on Housing of the House Comm. on Banking and Currency*, 93d Cong. 49 (1973) (testimony of Rep. Stephens) (explaining that the provisions in the proposed legislation pertaining to the reasonableness of settlement fees were eliminated).

The legislative history demonstrates that Congress did not intend for the legality of payments such as a yield spread premium to be dependent on the reasonableness of a broker's total compensation. The test Congress enacted in RESPA was whether the broker performed legitimate services in connection with each payment received, hence the fee "for" service language in § 8(c) and the fee for referral language, *i.e.*, "pursuant to," of § 8(a). Any other interpretation would fly in the face of Congress's clear intent to outlaw kickbacks and referral fees. Although Congress clearly rejected rate-setting measures, HUD has now tried to provide for rate setting through its "reasonable" overall payment analysis. Moreover, HUD is attempting to implement rate setting through an informal policy statement regarding an earlier informal policy statement, neither of which had the benefit of notice-and-comment rulemaking. Instead, HUD's 2001 Policy Statement was developed behind closed doors and without the required opportunity for the public to be heard.

The Fourth Circuit has rejected a similar attempt by HUD, in the same 2001 Policy Statement at issue here, to impose a reasonableness test on RESPA § 8(b). *See Boulware*, 291 F.3d 261. That court found that "RESPA was meant to address certain practices, not enact broad price controls." *Id.* at 268. Under HUD's interpretation, however, a single service provider would be liable for violating RESPA § 8(b) only "when it charges a fee that exceeds the 'reasonable' value of goods, facilities, or services provided" — an inquiry that necessarily requires a determination of the appropriate maximum rate for those services. *Id.* at 267 (internal quotation marks omitted).

III. CLASS ACTIONS ARE BOTH APPROPRIATE AND NECESSARY TO REMEDY AND DETER VIOLATIONS OF RESPA

Without the enforcement mechanism of class action lawsuits, RESPA § 8(a) would become entirely ineffective. Criminal prosecutions for violations of § 8(a) are non-existent. Individual suits cannot effectively eliminate unlawful referral payments. Borrowers are not likely to find counsel willing to pursue litigation over a claim with an average value of less than $2,500.[9] Class actions are essential, therefore, to the effective enforcement of RESPA. Without this method of private enforcement, unlawful charges will continue with the result that the ability of many Americans to own their own home will be impaired.

Class actions serve an important function in our judicial system and can be a major force for economic justice. *See Standards and Guidelines for Litigating and Settling Consumer Class Actions*, 176 F.R.D. 375 (1997). They often provide the only effective means for challenging wrongful business conduct, stopping that conduct, and obtaining recovery of damages caused to the individual consumers in the class. Frequently, many consumers are harmed by the same wrongful, standard corporate practice.

Here, Respondents' questioned conduct affects hundreds or even thousands of borrowers. A handful, or even a hundred filed individual suits, could not deter Respondents from their current lucrative practice of paying for referrals and driving up the costs of home ownership. A class action

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[9] It would be naive to think that RESPA's provision for attorney's fees would be sufficient to sustain consumers' rights. RESPA provides only that a "court *may* award to the prevailing party . . . costs . . . [and] *reasonable* attorneys' fees," 12 U.S.C. § 2607(d)(5) (emphasis added), which is far from the guarantee of recovery of an attorney's actual costs that would be needed to take on the considerable task of seeking remedies under RESPA with so small an amount at stake in any individual claim. Indeed, despite the prevalence of yield spread premiums in the mortgage industry, there have been few, if any, individual RESPA cases filed throughout the country.

is also the only means of efficiently redressing so many small claims. Hundreds of thousands of claims can be finally resolved in one action, one series of depositions and motions, and one trial. Individual actions are usually impracticable because the individual recovery would be insufficient to justify the expense of bringing a separate lawsuit.

Without class actions, businesses would be able to profit from their misconduct and retain their ill-gotten gains. *Id.* at 377. Class actions by consumers aggregate their power, enable them to take on economically powerful institutions, and make wrongful conduct less profitable. *Id.* The class action device is an extremely important vehicle for protecting consumers and holding corporate interests responsible for the harm that they do. *Id.* It also provides the only realistic mechanism by which injured persons can obtain injunctive relief to prohibit further illegal practices that would harm others.

As this Court recognized in *Deposit Guaranty National Bank v. Roper*, 445 U.S. 326, 338 n.9 (1980), without the prospect that individuals can reduce their costs of litigation and their attorneys' fees by allocating them among all class members who benefit from any recovery, unlawful yield spread premiums are unlikely to be challenged. The time and expense necessary to undertake such an action far exceed the value of any potential individual recovery even if the amounts are trebled. For that reason, homeowners who are charged unlawful yield spread premiums are unlikely to obtain legal redress at an acceptable cost unless they can proceed on behalf of a class of those similarly situated. *See Amchem Prods., Inc. v. Windsor*, 521 U.S. 591, 617 (1997) ("Advisory Committee had dominantly in mind vindication of 'the rights of groups of people who individually would be without effective strength to bring their opponents into court at all'") (citation omitted).

This very concern was repeatedly expressed during congressional hearings on RESPA with regard to the lack of

power that an unsophisticated homeowner holds against the mortgage industry:

> The individual, untutored, inept, fragmented homeowner does not have the leverage that the savings and loan institutions, the banks, the other institutions that are lenders, have in dealing with the real estate establishment to get these settlement costs decreased, to get the premium for title insurance decreased, to do away with kickbacks, to do away with all of these other matters that add to higher settlement costs.

Real Estate Settlement Costs, FHA Mortgage Foreclosures, Housing Abandonment, and Site Selection Policies: Hearings on H.R. 13337 Before the Subcomm. on Housing of the House Comm. on Banking and Currency, 92d Cong. 576 (1972) (testimony of Earl A. Snyder, University of Maryland).

Moreover, a recent Urban Institute Study financed by HUD reveals that minorities are most harmed by the leverage that lenders and brokers possess.[10] This study found that "[t]here is no question that minorities are less likely than whites to obtain a mortgage financing and that, if successful, they receive less generous loan amounts and terms." HUD News Release, No. 99-191, *New Reports Document Discrimination Against Minorities by Mortgage Lending Institutions* at 1 (Sept. 15, 1999). The Urban Institute Study also found that African-Americans and Hispanics tend to pay higher yield spread premiums than whites and that women pay more than men. *See* Urban Institute Study at 95 n.11. This study confirms Professor Howell Jackson's finding that African-Americans and Hispanics who obtained loans paid substantially more in closing fees and costs than other borrowers.[11]

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[10] *See Mortgage Lending Discrimination: A Review of Existing Evidence* (Turner & Skidmore eds., 1999) ("Urban Institute Study").

[11] "For African Americans, the average additional charge was $474 per loan, and for Hispanics, the average additional charge was $580 per

The minute power and resources of borrowers compared to lenders makes the use of the class action mechanism particularly appropriate.

IV. HUD'S 2001 POLICY STATEMENT DEPRIVES CONSUMERS OF ANY INPUT INTO THE RULE-MAKING PROCESS AND SHOULD NOT BE GIVEN DEFERENCE BY THE COURTS

The purpose of both the negotiated rulemaking process and notice-and-comment rulemaking is to allow consumers, business interests, and other interested persons to have input into an agency's regulations. *Amici* represent constituents who traditionally have little political power and whose right to be heard in administrative procedures that lead up to the promulgation of rules is of special importance. Consumer groups, including these *amici*, have consistently expressed concern at the industry's efforts to legalize predatory lending practices. Testimony at one recent Senate Committee hearing on predatory lending practices was replete with statements from persuasive witnesses that HUD's unilateral action in its 2001 Policy Statement had opened the door to the abusive use of yield spread premiums. Chairman Paul Sarbanes of the Senate Banking Committee presided over the hearings, including the hearing that specifically addressed the abuse of the yield spread premiums. Senator Sarbanes noted during the hearing that the reasonableness test found in HUD's 2001 Policy Statement "undercuts" the "plain language of the law, the regulations, the 1998 Congressional instructions to HUD . . . , and the 1999 HUD Policy Statement . . . [which]

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loan." *Predatory Mortgage Lending Practices — Abusive Uses of Yield Spread Premiums: Hearing Before the Senate Comm. on Banking, Housing, and Urban Affairs* (Jan. 8, 2002) ("2002 Senate Hearing") (Prepared Statement of Prof. Howell E. Jackson, Finn M.W. Caspersen and Household International Professor of Law and Associate Dean for Research and Special Programs, Harvard Law School ("Jackson's Statement"), *available at* http://www.senate.gov/~banking102_01hrg/010802/index.htm).

all make it clear that RESPA was intended to prohibit all payments that are not . . . for actual services provided." 2002 Senate Hearing, Tr. 5-6, 101; *see also id.* at 99-100 (Congress refused to grant HUD the authority to determine the reasonableness of fees when "they passed the legislation"); *id.*, Opening Statement of Chairman Paul S. Sarbanes, *available at* http://www.senate.gov/~banking/02_01hrg/010802/sarbanes.htm.

Representatives of the Mortgage Bankers Association ("MBA") and the National Association of Mortgage Brokers conceded during the hearing that it would be impossible for HUD to judge the "reasonableness" of individual yield spread premium payments. 2002 Senate Hearing, Tr. 100. Professor Howell E. Jackson of the Harvard Law School testified, "[W]hat we discovered [in the empirical study of Respondents' loan transactions] is the vast majority of yield spread premiums goes simply to increase the compensation of mortgage brokers. They do not go to reduce up-front costs." *Id.* at 82; *see also id.*, Jackson's Statement (Pet. App. 191a). Testimony also revealed that HUD was sorely misinformed as to the actual use of yield spread premiums by lenders such as Respondents. *See* 2002 Senate Hearing, Tr. 39-47.

HUD's "behind closed doors" formulation of the 2001 Policy Statement effectively circumvents the formal rulemaking process mandated by the Administrative Procedure Act ("APA"). HUD did not have authority under the APA to issue a policy statement that effected a change in the law without affording the public an opportunity to comment. *See* 5 U.S.C. §§ 551 *et seq.*

It is also clear that HUD's action came as the result of pressure from the industry, with no corresponding opportunity by consumers and the general public to have any input. *Amici* have learned that the MBA, an agent and representative of and lobbyist for lenders, lobbied HUD, after the publication of the Eleventh Circuit's *Culpepper III* decision, to strike the "for" language of the RESPA statute

and HUD's 1999 Policy Statement in its proposed 2001 Policy Statement. Indeed, the MBA provided HUD with a redlined version of HUD's 1999 Policy Statement, from which it struck out all of HUD's references requiring the lender making a payment "for," or in exchange for, services that the broker provided to the lender. *See* Pet. App. 112a-154a. The request for these changes refutes any claim that either the 1999 or the 2001 Policy Statement created a settled interpretation of RESPA. There is simply no way to reconcile HUD's 2001 interpretation with the 25 years in which HUD consistently concluded that referral payments are illegal under RESPA § 8(a) regardless of whether the total compensation received by the referring party is "reasonable."

Even if HUD's 2001 Policy Statement could be squared with the plain meaning of the statute, which it cannot, there is no congressional delegation of authority that could conceivably entitle HUD's Policy Statement to *Chevron* deference under these circumstances. *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The 2001 Policy Statement did not derive from HUD's delegated lawmaking powers; rather, it was a unilateral fix to stop a growing number of class action lawsuits. When an agency utilizes such informal means of interpreting regulations, its pronouncements are not entitled to the deference afforded to pronouncements that derive from delegated lawmaking powers. *Martin v. Occupational Safety & Health Review Comm'n*, 449 U.S. 144, 157 (1991). The fact that HUD here has encroached on matters traditionally assigned to the Judicial Branch in interpreting the scope of private rights of action is all the more egregious. *See Adams Fruit Co. v. Barrett*, 494 U.S. 638, 649-50 (1990); *see generally* Pet. 16-18.

Likewise, HUD's 2001 Policy Statement does not comport with the factors set out in *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944). The 2001 Policy Statement is glaringly inconsistent with HUD's previous administrative interpretations regarding what constitutes a violation of

RESPA § 8(a). Until 2001, HUD had consistently asserted that a payment made in exchange for the referral of business was illegal, period.

When viewed through the prism of HUD's repeated inability to promulgate regulations under RESPA § 8(a), it becomes even clearer that HUD succumbed to pressure from the industry and adopted informally what it could not promulgate through the procedures prescribed in the APA. HUD has not materially revised the regulations at issue here since 1992, when it concluded a four-year-long rulemaking, with new regulations that, among other things, required yield spread premiums to be disclosed on the federally mandated HUD-1 disclosure form. *See* 24 C.F.R. Pt. 3500. In response to industry objections that yield spread premium disclosure would be confusing to borrowers, HUD conducted a negotiated rulemaking from December 1995 to May 1996 designed to reach a consensus among consumer groups and the mortgage industry regarding the legality of yield spread premiums under RESPA. *See Real Estate Settlement Procedures Act (RESPA) Disclosure of Fees Paid to Mortgage Brokers; Proposed Rule and Notice of Proposed Information Collection Requirements*, 62 Fed. Reg. 53912, 53913-15 (1997) ("Proposed Rule"). Consumer groups, including NACA, participated in the negotiated rulemaking.

During the negotiated rulemaking, the consumer groups proposed a regulation that would have allowed lenders to pay yield spread premiums so long as the yield spread premiums were paid pursuant to express agreements between brokers and borrowers containing certain terms and disclosures. The proposed agreement would have stated the broker's total compensation both in dollars and as a percent of the amount financed. The mortgage industry objected, and advocated a rule that would require only disclosing "direct" fees (*e.g.*, loan origination fees) and classifying a transfer of a table-funded loan as a secondary market transaction. *See* Proposed Rule, 62 Fed. Reg. at 53917. Under the mortgage industry's proposals, yield

spread premiums paid in connection with table-funded loans would be *per se* legal.

This attempt by HUD to conduct a negotiated rulemaking failed. As a result of its efforts, however, HUD concluded that "there is confusion in the minds of consumers on the functions of mortgage brokers and the sources of their fees," resulting in higher costs to consumers. *Id.* at 53913. HUD then proposed a rule that would have created a qualified "safe harbor" for lenders that paid a yield spread premium pursuant to an "honest lending contract." By virtue of this contract, the borrower would expressly authorize the lender to make a yield spread premium payment as additional compensation for the broker's services. *Id.* at 53921-22. Again, because of numerous mortgage industry objections, the proposal to impose "an honest lending contract" was not adopted.

Because HUD changed its mind and did not accord the public any formal mechanism for input, the 2001 Policy Statement is not entitled to any deference, and the Eighth Circuit's decision relying on it exclusively to decertify the class should be reversed. For the Eleventh Circuit to have invoked the 2001 Policy Statement to overrule *Culpepper III* is detrimental and deeply offensive to the interests of millions of consumers throughout the country.

CONCLUSION

Amici respectfully urge this Court to grant the petition.

Respectfully submitted,

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